

TESTIMONY OF EDDY W. HARTENSTEIN

President, DIRECTV, Inc.

February 12, 1998

Thank you for inviting DIRECTV to participate in today's hearing. I want to thank you, Mr. Chairman, for introducing the bill which is the subject of today's hearing. I also want to thank Senator Burns, Chairman of the Subcommittee on Communications, for joining you in introducing that bill. As Senator Burns knows, more than 28% of Montana's residents have satellite dishes -- the greatest penetration rate of any state in the nation.¹ I also want to thank Senator Dorgan for his original cosponsorship of

S. 1422, and Senators Brownback, Hutchison, Inouye and Bryan for cosponsoring the legislation.

When DIRECTV® launched its service three and one-half years ago -- the culmination of ten years of effort and a \$750 million investment -- DIRECTV was dedicated to providing consumers with a compelling multichannel video alternative to incumbent cable television operators. DIRECTV today remains dedicated to that same goal.

DIRECTV has experienced strong growth since its inception, and is the leading provider of direct broadcast satellite ("DBS") service in the United States with more than 3.3 million subscribers. Today, one in every 30 households in the United States has DIRECTV. We achieved record subscriber growth in each month of the fourth quarter of 1997, and had our best month ever in December. While January typically is one of the slowest sales months for the consumer electronics industry, last month we recorded our best January ever. The Federal Communications Commission ("FCC") recently determined that DBS providers have a higher combined subscribership than any other multichannel video alternative to incumbent cable systems.²

¹ SkyREPORT.COM, Jan. 1, 1998.

² *Annual Assessment of the Status of Competition in Markets for the Delivery of Video*

Yet, as the FCC reported last month, 87% of multichannel video subscribers continue to receive service from their local franchised cable operator.³ We are targeting every one of those cable subscribers. We hope to convince them that DIRECTV offers a superior product at a competitive price. In fact, last week we launched a new marketing campaign targeting 18 cities in which residents have faced yet another round of significant cable rate hikes. A copy of an ad that has appeared in newspapers in those cities is attached as Exhibit A.

In our first year of operation, only 36% of our new subscribers lived in homes passed by cable and only 37% of our subscribers were cable subscribers at the time they became DIRECTV subscribers. In 1997, 73% of the subscribers we added lived in homes passed by cable and 55% percent of those new households subscribed to cable at the time they became DIRECTV subscribers.⁴ So we clearly are making significant inroads among cable subscribers.

We have taken a number of steps recently to make DIRECTV an even more attractive alternative to cable. DIRECTV added 18 networks to its lineup last year. Beginning March 10, DIRECTV will add eight more channels to its most popular programming packages, including MTV, Nickelodeon, TV LAND, VH1, Comedy Central and Lifetime. These channels will be added at no additional cost to subscribers. The addition of these channels will enable DIRECTV to offer the most complete lineup of popular cable channels, sports and pay-per-view movie entertainment available.

This spring, DIRECTV will begin offering a broad range of ethnic and foreign language programming using capacity we have leased on PanAmSat's Galaxy III-R satellite. In addition to serving underserved consumer segments, we will use this capacity to offer special interest and niche programming and future business-to-business applications. Galaxy III-R also will serve as an additional platform for the

³ *Id.* ¶ 7.

⁴ Based upon a random sampling of new and current DIRECTV subscribers taken every

launch of high definition television programming later this year.

Unfortunately, our efforts to compete aggressively with cable, and to provide the kind of competition that Congress wants us to provide, are being hampered by a number of regulatory and statutory obstacles. Most prominently, last fall the Librarian of Congress adopted an arbitration panel's recommendation of a startling and wholly unjustified increase in copyright fees for the retransmission of superstation and broadcast network affiliate signals to satellite television homes. Even more shocking is that the copyright fee satellite carriers are being asked to pay for network affiliate signals is more than **10 times** the amount that cable operators pay for the exact same signals. The reversal of this decision to penalize Americans who have chosen an alternative to cable television is of extreme importance to DIRECTV and the entire DBS industry. It is having a detrimental effect on the ability of DBS operators to compete aggressively with cable.

Satellite carriers pay copyright fees to a royalty pool maintained by the U.S. Copyright Office for the right to retransmit superstation and network affiliate signals to consumers. The fees are used to compensate owners of the copyrighted programming carried on those retransmitted signals.

The Satellite Home Viewer Act⁵ provides that satellite copyright rates are to be determined through negotiations between the satellite carriers and the copyright owners. If the negotiations are not successful, as in this case, a Copyright Arbitration Royalty Panel ("CARP") is convened to conduct a mandatory arbitration.

For more than 5 years, the satellite carriers' copyright rates were 14 cents per subscriber per month for each superstation signal, and 6 cents per subscriber per month for each network affiliate signal. Last August, a CARP recommended that satellite carriers pay 27 cents for all signals. Despite the opposition of more than 60 Members of Congress, the Librarian of Congress adopted this recommendation.⁶

Cable operators also pay copyright fees for the retransmission of broadcast signals, but cable's rates are determined by statute rather than by arbitration. Cable's rates are dramatically lower than satellite's, an average of 9.8 cents for superstations and 2.45 cents for network signals, as shown on Exhibit B. This enormous disparity in the copyright fees paid for the exact same signals is completely unjustified.

The irrationality of this decision becomes even more apparent when one looks at the total amounts expected to be paid into the copyright royalty pools by satellite

⁵ 17 U.S.C. § 119.

⁶ *In the Matter of 1996 Satellite Carrier Royalty Rate Adjustment Proceeding*, Final Rule d. Reg. 55742 (October 28, 1997). The Librarian of Congress did, however, reject the CARP's recommendation that the fee instead set a January 1, 1998 effective date.

On September 11, 1997, the satellite carriers filed with the Librarian of Congress a motion for a stay of the Order adopting the fee increase. The motion asked the Librarian to delay the effective date of the rate increase so as to give Congress sufficient time to examine the effect on video competition which will result from the fee increase. The Librarian rejected the motion for a stay on November 14, 1997.

The satellite carriers have filed an appeal with the United States Court of Appeals for the District of Columbia Circuit. *Satellite Broadcasting & Communications Association v. The Librarian of Congress*, Case No. 97-1659. The court denied a motion to stay the effective date of the Librarian's determination on December 22, 1997.

carriers and cable operators. Satellite carriers, which today serve 8.5 million households,⁷ contributed approximately \$37 million in copyright fees in 1997. Based upon a projection of 10 million households in 1998, satellite carriers will contribute approximately \$97 million in copyright fees in 1998, \$60 million more than they paid in 1997.⁸ Cable operators, which today serve approximately 65 million households, contributed approximately \$170 million in copyright royalties in 1997. It is projected that cable will serve approximately 66 million households in 1998.⁹ Thus, even assuming cable's copyright contributions remained constant, satellite carriers, which will serve 15% of the households served by cable, will be contributing 57% of the copyright fees contributed by cable in 1998. This strikes me as a perfect example of bureaucratic taxation without representation.

We are not saying that we should not have to contribute to the copyright royalty pool. All we are saying is that at a time when Congress and the FCC are attempting to foster competition to cable, there is absolutely no justification for the DBS industry to pay higher copyright fees than the cable industry pays for the exact same signals.

I would note that it seems somewhat ironic to me that Mr. Valenti and I are on opposite sides of this issue. DBS has been a huge, new revenue source for the movie studios. Our pay-per-view buy rates significantly surpass those of any of our multichannel video competitors. Since every time we sign up a new subscriber Mr. Valenti's members profit, I would have hoped that the MPAA would share our concerns about the effects that this rate increase will have on our ability to grow this important new source of studio revenues.

As a result of the Librarian's decision, we felt we had no choice but to increase our price for network signals by 21 cents per signal, the exact amount of the copyright fee increase. What does this mean to our subscribers? If a subscriber receives the maximum of eight network signals, his or her monthly bill for this programming package has increased a whopping 34%.

I have heard some suggest that an increase of \$1.68 per month isn't a big deal. I think that's a very elitist view. That's twenty dollars a year that the government has taken from a family. In fact, one of our cable competitive programming packages, Select Choice®, is \$19.99 per month. That additional twenty dollars is like charging subscribers for an extra month's worth of programming. So I reject the notion that we shouldn't be concerned about the copyright fee increase because of the amount of money involved.

⁷ *DBS Companies Report Solid Numbers for January*, SkyREPORT.COM News, Feb. 9,

⁸ Satellite Broadcasting and Communications Association estimates.

⁹ Paul Kagan, *The Cable TV Financial Databook*, at 10 (1997).

Moreover, Congress' original intent in establishing the satellite compulsory license was to make network programming available to consumers who live in areas of the country where they are unable to receive over-the-air signals from their local network affiliates. Unfortunately, this consumer-friendly objective has been compromised by the Librarian's decision to establish such an excessive copyright rate.

There is no reason why satellite TV subscribers should be burdened with higher fees than cable subscribers for the exact same network affiliate programming. Not only does this fee discriminate against satellite TV subscribers, it also discriminates against rural residents who are more heavily affected by the fee increase.

S. 1422, and the companion House bill, H.R. 2921, would give satellite TV subscribers a temporary reprieve from this discriminatory differential in copyright fees. It will give Congress the time it needs to revise the law to ensure that satellite TV subscribers are treated equitably in the future. The simplest way to do that is establish a statutory rate for satellite copyright fees that is comparable to the rate currently paid by cable operators. I would note that FCC Chairman William E. Kennard has suggested such a legislative change.¹⁰

Let me assure you that should Congress roll back the copyright fee increase, DIRECTV promptly will cancel the price increase as of the effective date of the change. Moreover, we will credit accounts for amounts paid to DIRECTV as a result of the fee increase to the extent that the bill overturning the increase applies to fees already

¹⁰

1977 Report, Separate Statement of Chairman William E. Kennard, at 5.

collected. In fact, I already have made this pledge in a letter to our network signal subscribers dated November 25, 1997.

S. 1422 also would direct the FCC to report to Congress on the effect of the increase in royalty fees paid by satellite carriers on multichannel video programming competition and on the ability of the satellite industry to compete in that marketplace. We certainly would welcome such a study by the FCC. But I can predict with some confidence that the FCC will conclude that the disparity in copyright rates has a significant impact on competition. In fact, last month the Commission recommended that the "existing differences between the copyright treatment of cable transmissions and of satellite retransmissions of broadcast signals should be removed where possible so that the compulsory licenses do not affect the competitive balance between the satellite carrier and cable industries."¹¹

Let me be clear that the satellite compulsory copyright license has been enormously significant to DBS providers such as DIRECTV. The license has been and remains absolutely necessary to alleviate the enormous copyright clearance burden that otherwise would be experienced by DBS providers in its absence -- a particularly onerous burden for start-up competitors to cable incumbents.

However, the satellite compulsory license also has been responsible for disadvantaging DBS providers in the multichannel video marketplace: First, even prior to this most recent substantial increase, satellite carriers have paid copyright fees significantly higher than those paid by cable operators for the exact same broadcast signals.¹² Second, the compulsory license for cable operators is a permanent license, whereas the satellite license has been subjected to a series of sunsets and renewals, and currently is set to expire on December 31, 1999.¹³ Third, current cable subscribers are required to drop their cable service and wait a period of ninety days before they can subscribe to satellite-delivered network affiliate signals. Fourth, the satellite compulsory license currently applies only to "private home viewing." The cable license has no such restriction. Finally, unlike cable operators, which have no restrictions on their ability to offer broadcast signals to their subscribers, DBS providers are precluded from offering network affiliate signals to their subscribers in most areas of the country.

These unfair and anti-consumer disparities should be remedied so as to place DBS operators on a more equal footing with their entrenched cable competitors.

At the beginning of my testimony, I mentioned that we are being hampered by a number of regulatory and statutory obstacles. I would be remiss if I did not briefly identify the other obstacles to which I was referring.

First, it is uneconomical for consumers who wish to receive only their local broadcast channels via cable and the rest of their programming via DBS or another alternative provider to do so when they are required to pay more than \$20 per month for basic cable. The solution is simple: cable systems should be required to offer a low-cost, "local broadcast only" programming package that it is available to all

¹¹ *Id.* ¶ 247.

¹² See 17 U.S.C. § 111.

¹³ The Copyright Office agrees "that the satellite carrier industry should have a

consumers. In an FCC hearing on December 18, 1997, Decker Anstrom, President of the National Cable Television Association, acknowledged that this is an idea worth examining.

Second, I would urge Congress to extend the program access law beyond the year 2002, when it currently is set to expire, as well as to clarify that the law's protections apply to all programming in which a cable operator has an attributable interest, regardless of the distribution method employed.

Finally, the proposed DBS alliance between Primestar, an entity controlled by the nation's five largest cable operators,¹⁴ and News Corp., a company that calls itself "the world's most vertically integrated media company,"¹⁵ will serve only to strengthen cable's dominance and to weaken its competitors. There is every reason to believe, based on Primestar's past performance as a medium-power direct-to-home satellite service, that the Primestar-News Corp. entity will use the national distribution capabilities of high-power DBS to complement, rather than compete with, cable service. Thus, permitting the nation's five largest cable operators to control one of only three DBS orbital locations capable of providing service to the entire continental United States will undermine Congress' interest in ensuring that this scarce asset is used to attack, rather than bolster, cable's market dominant position.

I appreciate the opportunity to testify at this hearing. I want to reiterate my thanks to those of you who have been so supportive, especially Senators McCain,

¹⁴ Primestar's MSO owners are: TCI, Time Warner, MediaOne (formerly Continental

¹⁵ News Corp. 1996 Annual Report.

Burns and Dorgan. I hope those of you who have not yet cosponsored S. 1422 will considering joining your colleagues in their efforts to overturn the inequitable satellite copyright fee increase. I believe that rectifying this anti-consumer bureaucratic action will advance the public interest in the development of robust multichannel video competition.